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Affiliation: Centre for Real Estate Studies, Universiti Teknologi Malaysia, Johor, Malaysia

Keywords: Economic Thought; Heritage; Market Value; Property Transaction; Real Estate; Sustainable

Received: April 11, 2022 | **Accepted:** June 30, 2022

Type of Paper: Review | **Vol.** 10(2) **Page:** 72-76

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Received: April 19, 2022 | **Accepted:** June 30, 2022

Determinants of Earnings Management Actions in Indonesian Banking Companies

Arna Suryani, Ariayani

Batanghari University, Jambi, Indonesia

Abstract

Objective - This study aims to examine the influence of Investment Opportunity Set and Corporate Social Responsibility Disclosure through Profitability on Earnings Management. The companies examined are banking companies listed on the LQ45 Index of the Indonesia Stock Exchange (IDX).

Methodology – This study used data sourced from annual financial reports of banking companies on the LQ45 Index of the Indonesia Stock Exchange for the 2016-2020 periods. This study used descriptive and verification analysis methods with path analysis and hypothesis testing. Investment Opportunity Set is measured by Market Value to Book Value of Assets, Corporate Social Responsibility Disclosure is measured by Global Reporting Initiative G4 indicators, Profitability is measured by Return on Assets, and Earnings Management is measured by Discretionary Accruals.

Findings – The results indicate that Investment Opportunity Set and Corporate Social Responsibility Disclosure and Profitability have no effect on Earnings Management. This implies that Earnings Management actions in companies are more likely to be influenced by other variables which closely related to agency theory and hard to predict the determinants by using only several variables.

Novelty – Based on the results of this study, Profitability as an intervening variable does not mediate the effect of Investment Opportunity Set and Corporate Social Responsibility on Earnings Management. This might happens because profitability is quite common for investors and users of financial

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GATR Journal of Finance and Banking Review
Vol. 7 (1) April - June 2022
Issue DOI: 10.35609/jfbr.2022.7.1

GATR JOURNALS
Suite 15, Taman Bukit Angkasa, Jalan Pantai Dalam, 59200, Kuala Lumpur, Malaysia

Content

GATR Journal of Finance and Banking Review
GATR JOURNALS
Journal homepage: http://gatrenterprise.com/GATRJournals/JFBR/vol7_2022_issue1.html
J. Fin. Bank. Review 7(1) 39–50 (2022)

Determinants of Earnings Management Actions in Indonesian Banking Companies

Arna Suryani[1*], Ariayani[2]

[1,2]Batanghari University, Jambi, Indonesia

ABSTRACT

Objective – This study aims to examine the influence of Investment Opportunity Set and Corporate Social Responsibility Disclosure through Profitability on Earnings Management. The companies examined are banking companies listed on the LQ45 Index of the Indonesia Stock Exchange (IDX).

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Novelty - Based on the results of this study, Profitability as an intervening variable does not mediate the effect of Investment Opportunity Set and Corporate Social Responsibility on Earnings Management. This might happens because profitability is quite common for investors and users of financial statements in assessing the company's financial performance so that it is easier for users of financial statements to know the Earnings Management actions done by the company.

Type of Paper: Empirical

JEL Classification: G11, G20.

Keywords: Bank; Investment Opportunity Set; Corporate Social Responsibility; Profitability; Earnings Management.

Reference to this paper should be made as follows: Suryani, Arna. Ariayani. (2022). Determinants of Earnings Management Actions in Indonesian Banking Companies, *J. Fin. Bank. Review*, 7(1), 39 – 50. https://doi.org/10.35609/jfbr.2022.7.1(2)

1. Introduction

Along with the development of economy, one of the industries that is growing and is in great demand by investors is banking. The bank acts as an intermediate institution between parties who have excess funds with parties who need funds. The important role of banks gives a great contribution to country's economic growth.

* Paper Info: Revised: April 19, 2022
Accepted: June 30, 2022

* Corresponding author: Arna Suryani
E-mail: arna_halim@yahoo.co.id
Affiliation: Faculty of Economics, Batanghari University, Jambi, 36122, Indonesia

Just like any other company, a bank's goal is to get the maximum profit possible to attract investors. Generally, investors see profit as the main point as a measure of the success of a company. Investors tend to put funds in entities that have high profits and growth (Dang et al., 2017). A company's profit reflects the company's financial performance, and growth prospects and determines the amount of tax that has to be paid.

The importance of the meaning of earnings encourages managers to intervene in earnings through "Earnings Management" for certain interests that benefit the company (Becker et al., 1998). Watt and Zimmerman (1990) in Suryani & Herianti (2015) defined earnings management as the action of a manager in using accounting policies to report accounting numbers that are not in accordance with the actual economic conditions of the company and mislead investors in making decisions.

So far there has been no prohibition on earnings management in the company except those related to taxes. Therefore, there are still many arguments about earnings management behavior is allowed or not in a company. In this study, researchers think that earnings management actions are still inappropriate in the company because it means that the company does not provide open and transparent information to stakeholders and can influence various economic decisions. Moreover, the role of banks as agents of trust in society is certainly expected to be able to provide transparent financial information in accordance with the conditions of the bank itself.

There are various financial aspects that are thought to intervene in profits such as Investment Opportunity Set (IOS). The IOS of a company gives influences on the perceptions of managers, owners, investors and creditors of the company (Kallapur & Trombley, 2001). IOS is suspected to be one of the factors that encourage companies to do Earnings Management. If the prospect of the company shown by IOS showed unfavorable results, of course this will give a negative signal to investors towards the company. Managers usually do not want to lose funds from investors, so they take steps to be able to continue to retain investors, such as manipulating profits to improve the value of the company's prospects in IOS.

Not only from the company's profit and investment prospects that are observed by the public, but corporate social responsibility is also a spotlight for assessing a company. Corporate Social Responsibility sees how much awareness the company has about how its business decisions can give impact society (Suryani & Herianti, 2015). CSR activities are often used as an excuse for managers to practice earnings management. CSR carried out by the company will provide a positive value for the company because investors do not only look at the financial aspects in the financial reports, but investors also look at the company's image in the public to assess the company's feasibility to get funds. Besides the prospect of the company and the disclosure of corporate social responsibility, there is one factor that is suspected to encourage the managers to intervene in the earnings, which is profitability.

Profitability reflects the organization's capacity to obtain profits during a period and can measure organization's performance. Higher profitability indicates the company's ability to gain profits. Companies that get low profitability in a certain period will be encouraged to carry out earnings management to increase profits or maintain profit stability. Managers often try to manage profits to look good in the investors' eyes so that investors entrust their funds to the company. However, this kind of action will become misleading false information for investors because the financial reports do not show the real condition of the company.

The main purpose of this study is to determine what factors affect Earnings Management actions in banking companies listed on the LQ45 Index of the Indonesia Stock Exchange. This study is expected to contribute to the development of knowledge, particularly in the field of bank and finance, especially on the topic of earnings management. The research results are also expected to be used as a self-evaluation for bank management to provide reliable and transparent financial information for the stakeholders in making a critical decision and also as an early warning system for investors and regulators in assessing companies.

The introduction contains the background to the study. The literature review discusses the background theories related to the topic. The methodology outlines the research technique, the sampling, and the model used. The results convey the results of the statistical data processing. The discussion elaborates on the statistical data and the paper ends with a conclusion.

2. Literature Review

Earnings Management is a company management behavior to intervene or influence the information in the financial statements with the aim of deceiving stakeholders who want to know the performance and state of the company (Sulistyanto, 2008). Earnings Management provides flexibility for managers to protect themselves and the company in anticipating unexpected events for the benefit of the parties involved in the agreement. Watt and Zimmerman (Watts & Zimmerman, 1990) in Suryani & Herianti (Suryani & Herianti, 2015) defined Earnings Management as a manager's action in using accounting policies to report accounting numbers that are not in accordance with the actual economic conditions of the company and mislead investors in making economic decisions with the profit figures.

According to Scott (2003) cited by Suryani (2017), earnings management can be in form of taking a bath, income minimization, income maximization and income smoothing. Salno and Baridwan (2000, p. 19) stated that the concept of earnings management uses an agency theory approach which states that "earnings management practices are influenced by conflicts between the interests of management (agent) and owner (principal) that arise because each party tries to achieve or consider the desired level of prosperity. This conflict can arise due to the owner as the principal unable to monitor the daily management activities to ensure that the management as the agent works in accordance with the wishes of the shareholders.

The difference in information between management and company owners can provide an opportunity for managers to carry out earnings management which can mislead company owners about the company's economic performance. Agency theory raises problems caused by incomplete information or asymmetric information, namely when not all circumstances are known by both parties and as a result there are certain consequences that are not considered by both parties.

Basically, there are three approaches used to detect earnings management, namely the model based on aggregate accruals, specific accruals, and distribution of earnings after management (Sulistyanto, 2008). In this study, researchers used the first model based on aggregate accruals using discretionary accruals referring to the modified Jones model as a proxy for earnings management because the aggregate accruals model is in line with the accounting basis that has been widely used in various countries, namely accrual-based accounting which records all transactions based on the time they occur and not when cash is received or issued. Moreover, the accrual component in the financial statements is indeed a gap for managers when managing the earnings to be reported because managers have the freedom to choose and change accounting recording methods in accordance with the goals they want to achieve.

IOS is the combination of resources owned and future investment options with positive net present value. Investment options are chances to grow, but sometimes the company cannot always use all investment opportunities in the future. Companies will have higher expenditures compared to the value of lost opportunities if they cannot use investment opportunities (Astriani, 2014). Since IOS reflects how great the company's performance in managing their investment opportunities and will be observed by stakeholders, researchers believe that IOS will give impact the earnings management actions in company.

According to (Kallapur & Trombley, 2001) in measuring a company's prospects through IOS, there are three types of proxies namely based on price, investment and variance. In this study, the Investment Opportunity Set is proxied by a price-based proxy, namely Market Value to

Book Value of Assets. This ratio reflects a proxy that states that the company's growth prospects are partly expressed by market prices. Price-based proxies are based on the assumption that growing companies will have a higher market value relative to existing assets because growth prospects will at least be reflected in stock prices

Nowadays, Corporate Social Responsibility has become the main attraction of investors in assessing a company. Corporate Social Responsibility is an action by which organizations keep social concerns in mind for their business activities as well as in their cooperation with partners based on voluntary and associational standards (Nuryana, 2005). By communicating CSR activities, it is hoped that more people will know about the company's social activities and will reduce the risk of social turmoil. So that the company's social hedging value will increase by reporting CSR to the public (Harmoni & Andriyani, 2008).

Corporate Social Responsibility activities are related to legitimacy theory. According to Lindblom (1993), legitimacy is a condition where the value system of an entity is the same as the value system of the social system of society in which an entity is a part of society. This legitimacy theory can be applied to companies that carry out social responsibility activities. The impact of the company's activities will greatly affect the surrounding community so that what is done by the company will return to the community.

Therefore, the company's management needs support from a supportive community environment so that the company can operate calmly. In other words, companies need legitimacy from the surrounding community. This is also in line with the legitimacy theory which states that the company has a contract with the community to carry out its activities based on the values of justice, and how the company responds to various interest groups to legitimize the company's actions.

The dimension of CSR disclosure is in accordance with the concept of sustainability development in the sustainability report based on the Global Reporting Initiative (GRI G4) standard; there are 91 indicators, which are economic, environmental and social indicators. To make no gap between companies that make sustainability reporting and companies that do not, CSR calculations are carried out using a dummy variable, namely, Score 0: if the company did not disclose item in the indicator. Score 1: if the company disclosed the item on the indicator.

Since the company's main goal is to gain maximum profit, therefore profitability has also become a crucial factor for stakeholders in making economic decisions and even evaluating the company's performance in a certain period. According to Kasmir (2019, p. 327), profitability is the organization's ability to obtain profits within a period. Profitability is a top priority for investors before investing their funds. Profitability also provides an overview of the company's financial strength in the long term.

There are five proxies for measuring profitability ratio: Return on Assets, Return on Equity, Net Profit Margin, Gross Profit Margin, and Earnings per Share as stated by Hamidah (2015, p. 57). This study used Return on Assets to measure profitability. Return on Assets is a ratio that shows the rate of return on total assets after profit minus interest and taxes which shows the success of the company's asset performance in a certain period.

Companies with high IOS tend to have a high level of profitability because they are assumed to be able to manage company resources well. The implementation of CSR activities can increase the company's sales and will ultimately increase profitability. On the other hand, the company will get a positive image in the community when the company implements CSR well. This positive image is able to give positive benefits to company.

Research by Sari (2013) related to the effect of IOS on profitability using ROA shows a positive and significant effects. Musfirarti et al. (2021) stated that CSR disclosure has a positive and significant effect on profitability using ROA. Based on the description above, the hypotheses in this study can be formulated as follows.

H1: *IOS using Market Value to Book Value of Assets as indicator has a positive effect on Return on Assets as the profitability indicator.*

H2: *CSR has a negative effect on Return on Assets as the profitability indicator.*

The investment Opportunity Set (IOS) of a company reflects the company's future growth projections. The IOS value is expected to show high company growth. When the IOS is low, managers are likely to intervene in earnings which can be detected with Discretionary Accruals to provide a good projection of the company's growth in the future and will give profits for investors. Disclosure of the company's Corporate Social Responsibility (CSR) activities is one of the information disclosures made by the company to third parties through annual financial reports. Earnings Management is the behavior of managers to intervene ithe net income reported in financial statements for certain purposes by using various strategies such as making CSR activities as the shield.

Research by (Irawan & Apriwenni, 2021b) showed that IOS has a positive and significant effect on Earnings Management while Kumala & Haryono (2004) stated that IOS has no significant effect on Earnings Management. Suryani & Herianti (Suryani & Herianti, 2015) stated that CSR disclosure has a positive and significant effect on Earnings Management. Research by Purnama (2017) showed that there is a positive and significant effect from Profitability on Earnings Management. In this study, we used Profitability as the intervening variable. Therefore, the research hypothesis can be formulated as follows.

H3: *IOS using Market Value to Book Value of Assets as indicator has a positive effect on Earnings Management.*

H4: *CSR has a positive effect on Earnings Management.*

H5: *Profitability using Return on Assets has a positive effect on Earnings Management.*

3. Research Methodology

This study used secondary data sourced from the annual financial reports of banking companies on index LQ45 of Indonesia Stock Exchange for 2016-2020 periods. This research is a census study, that is, all the population is sample. There are 5 banking companies on LQ45 of Indonesia Stock Exchange that used in this study. Researchers used descriptive and verification analysis methods and analysis tools using path analysis to find out the direct and indirect effects between the independent variable and the dependent variable. Researchers used the Statistical Package for Social Sciences (SPSS) program.

Before entering the path analysis test, the researchers tested the classical assumption, namely the normality test using One Sample Kolmogorof-Smirnov to test whether the residual values of the research variables are normally distributed or not (Ghozali, 2016). Researchers also test the hypotheses using t test.

This research is intended to analyze the influence of Investment Opportunity Set and Corporate Social Responsibility Disclosure through Profitability on Earnings Management in the banking companies listed on the LQ45 index of the Indonesia Stock Exchange periods 2016 - 2020. The independent variables in this study are Market Value to Book Value of Assets as X1 and Corporate Social Responsibility as X2. The variable dependent variable is Discretionary Accruals as Z with the intervening variable, namely return on Assets (Y). The conceptual framework can be seen below.

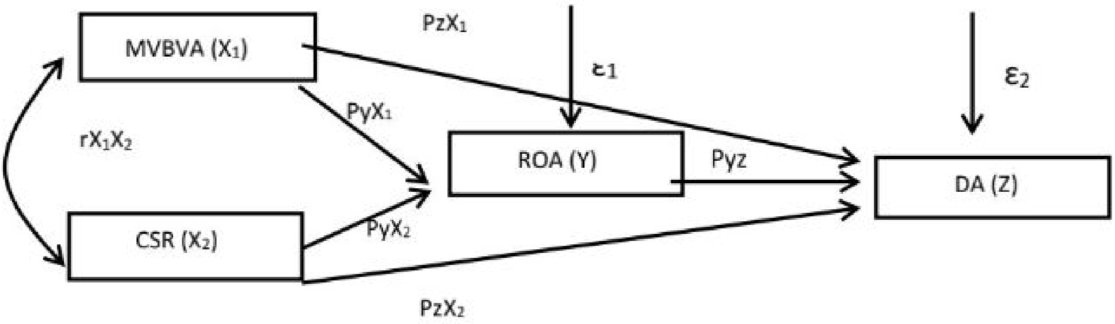

Figure 1. Conceptual Framework

Operational variables are definitions or descriptions that explain the variables to be studied and include the indicators that exist in each variable. With this explanation, the author will more easily measure the existing variables. The operational description of the variables in this study briefly is as follows:

Table 1. Operational Variables

Variable	Definition	Formula	Scale
Market Valueto Book Valueof Assets (X_1)	The development possibilities are showed by market prices (Kallapur & Trombley, 2001).	$\text{MVBVA} = \frac{(\text{T. assets} - \text{T. equity}) + (\text{Stocks x Stocks price})}{\text{T. assets}}$	Ratio
Corporate Social Responsibility (X_2)	An action when organizations keepsocial concerns in their businessactivities based onvoluntary standards (Nuryana, 2005).	$\text{CSR} = \frac{\text{Total of indicators disclosed}}{91}$	Ratio
Return on Assets (Y)	A profitability ratiothat shows return of total assets (Hamidah, 2015).	$\text{ROA} = \frac{\text{Profit after tax}}{\text{Total assets}} \text{x } 100$	Ratio
Earnings Management (Z)	Earnings management proxy uses the modified Jones model, namely total accruals andregression models to detect overallearnings management (Suryani, 2017).	**Step 1:** $TAC_{it} = N_{it} - CFO_{it}$ **Step 2:** $\frac{TAC_{it}}{A_{it-1}} = \beta_1\left(\frac{1}{A_{it-1}}\right) + \beta_2\left(\frac{REV_{it} - REV_{it-1}}{A_{it-1}}\right) + \beta_3\left(\frac{PPE_{it}}{A_{it-1}}\right)$ **Step 3:** $NDA_{it} = \beta_1\left(\frac{1}{A_{it-1}}\right) + \beta_2\left(\frac{\left([REV_{it} - REV_{it-1}] - [REC_{it} - REC_{it-1}]\right)}{A_{it}}\right) + \beta_3\left(\frac{PPE_{it}}{A_{it-1}}\right)$ **Step 4:**	Ratio

		$DA_{it} = \frac{TAC_{it}}{A_{it-1}} - NDA_{it}$	

4. Results

Before doing the path analysis test, a normality test was carried out using the Kolmogorov- Smirnov test, the result of the Asymp Sig value is 0,200 > 0,05 then the data is normally distributed so that the data in this study is feasible to use. All correlation coefficient probability values obtained are significant, namely sig. (2 tailed) > 0,05 indicates that the correlation of each variable is a significant relationship.

Simultaneous test results MVBVA and CSR have 58, 10% contribution to ROA. The results of data processing that tested the effect of MBVA and CSR on ROA based on path analysis obtained a direct effect of MVBVA on ROA is 12,60% and the value of the indirect effect of MVBVA through CSR on ROA is 11,35% and the total effect is 23,95%. The t count result is 1,912 and the significance level of 0,069 is greater than 0,05. It means that MVBVA has a positive and insignificant effect on ROA.

Meanwhile, the result of the path analysis of the direct influence of CSR on ROA is 22,8% and the indirect effect of CSR through MVBVA on ROA is 11,35% and the total effect is 34,15%. The t count result is -2,569 and the significance level of 0,018 is smaller than 0,05. It means that CSR has a negative and significant effect on ROA. Furthermore, the results of the analysis are also strengthened by the value of R Square (R2) which shows the contribution given by the MVBVA and CSR on ROA is 0,581 or 58, 10%.

The result of data processing that tested the effect of MVBVA, CSR, and ROA based on the results of path analysis obtained the direct effect of MVBVA on Earnings Management is 2,20% and the indirect effect of MVBVA through CSR on Earnings Management is 0,65% with total effect is 2,85%. The t-count result is -0,530 and the significance level of 0,601 is greater than 0,05. It means that MVBVA has a negative and insignificant effect on Earnings Management.

Meanwhile, the result of path analysis direct effect of CSR on Earnings Management is 0.40% and the indirect effect of CSR through MVBVA on Earnings Management is 0.65% with a total effect is 1,05%. The t count result is 0,231 and the significance level of 0,819 is greater than 0,05. It means that CSR has positive and insignificant effect on Earnings Management. Furthermore, the results of the analysis are also strengthened by the value of R Square (R2) which shows the contribution given by the MVBVA and CSR on Earnings Management is 0,039 or 3,90%.

From the path analysis also obtained the direct effect of ROA on Earnings Management is 2.20%. The t count result is 0,716 and the significance level of 0,481 is greater than 0,05. It means that ROA has positive and insignificant effect on Earnings Management. The following can be seen in Figure 2 the influence of MVBVA, CSR through ROA on Earnings Management.

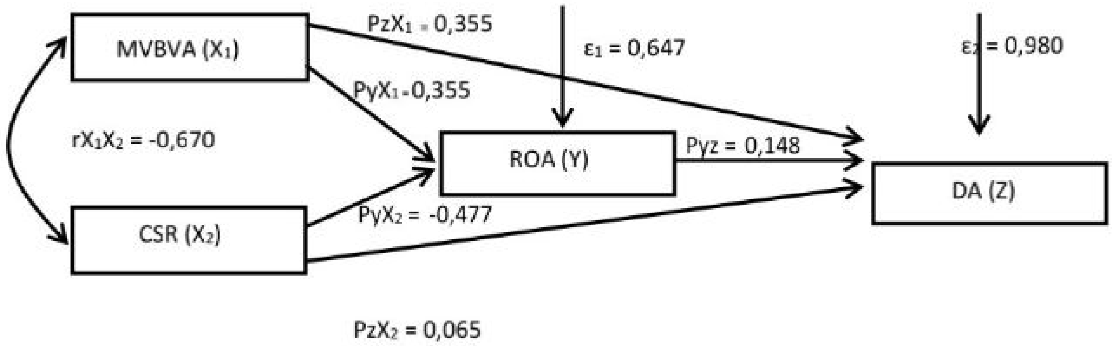

Figure 2. The influence of MVBVA, CSR through ROA on Earnings Management

The influence of MVBVA through ROA on Earnings Management has a direct effect PyX1.PzX1.Pyz = -0,80%, while indirect effect MVBVA through CSR and ROA on Earnings Management is PyX1.PzX1.rX1X2.PyX2.Pyz = -0,30%.

Then, the total effect is -1,10%. The direct effect of the influence of CSR through ROA on Earnings Management is PyX2.PzX.Pyz = -0,50%, while indirect effect CSR through MVBVA and ROA on Earnings Management is PyX2.PzX2.rX1X2.PyX1.Pyz = 0,11%. Thus, the total effect is -0,39%. The contribution of the influence of MVBVA through ROA on Earnings Management is -1,10%.

The contribution of the influence of CSR through ROA on Earnings Management is -0,39%. Thus, the total effect is -1,49%. Therefore, MVBVA and CSR through ROA gave negative contribution on Earnings Management. It means that Return on Assets as an intervening variable does not mediate the influence of Market Value to Book Value of Assets and Corporate Social Responsibility on Earnings Management.

5. Discussion

The results above proved that companies that have good prospects in the future are proxied by the MVBVA and have the awareness and social responsibility programs for the community can give a good impact on profitability. This result is in accordance with results from Sari (Sari, 2013) and Musfirati et al. (Musfirati et al., 2021) that stated IOS and CSR affect profitability as proxied by ROA. The combination of good corporate prospects with disclosure of corporate social responsibility programs does indeed provide a positive impact for the company on the public and attract investors because a good company prospect means that the company is able to optimally manage its business activities to increase profitability and corporate social responsibility activities make the community give a positive response to the company.

MVBVA has no significant effect on ROA in banking companies, presumably because predictions from company prospects with good value do not always mean high-value company profitability, as well as predictions from bad company prospects, also cannot determine company profitability because in that period there may be factors other factors that affect the level of profitability, such as leverage, liquidity, and assets turnover. Even though the MVBVA does not give a significant effect on profitability, it is crucial for managers to maintain the quality of company prospects as shown in MVBVA.

CSR has a negative effect on ROA because the implementation of social responsibility activities done by the company will increase the company's expenses and have an impact on profits for the period. However, CSR will give positive impact on society that is beneficial for the survival of the company as stated in the legitimacy theory which states that the value system of an entity is the same as the value system of the social system of society where an entity is part of the community. The impact of the company's activities will greatly affect the surrounding community so that what is done by the company will return to the community and again have an impact on the company itself.

The company's prospects as reflected in the MVBVA and the company's social concern for the community from CSR activities do not guarantee that the company will not carry out profit manipulation because it is suspected that there are other factors that can be associated with agency theory (Salno & Baridwan, 2000). Agency theory in the concept of Earnings Management has the view that the practice of profit intervention carried out by the company can be influenced by conflicts between the interests of management (agent) and owners (principals) that arise because each party tries to achieve or consider the level of prosperity they desire. Agency theory has the assumption that each individual is solely motivated by self-interest, causing a conflict of interest.

In an agency relationship, the principal does not have sufficient information about the agent's performance. Agents have more information about their capacity, work environment and the company as a whole. This result in an imbalance of information called information asymmetry. The assumption that individuals act to maximize themselves causes agents to take advantage of their information asymmetry to deceive the principal. Information asymmetry and conflicts of interest that occur encourage agents to present untrue information to the principal. One form of such action is Earnings Management.

ROA does not have a significant effect on earnings management in banking companies, these results support the research conducted by Karina & Sutandi (2019) which stated that the greater the level of ROA does not affect the company's management actions in intervening on earnings. This could happen because banking companies listed on the LQ45 index of the Indonesia Stock Exchange no longer rely on Return on Assets as a determinant of Earnings Management actions because the Return on Assets has been such a common ratio for assessing a company and the managers do not want stakeholders to easily know about the profit intervention. Therefore, managers will rely on other variables before doing the profit intervention.

The results in this study showed that profitability, as proxied by Return on Assets as an intervening variable, does not mediate the effect of MVBVA and CSR on Earnings Management. This is because the company sees other aspects other than ROA as a driver of Earnings Management actions because ROA is quite commonly monitored by investors or users of financial statements so that it can make it easier for users of financial statements to find out Earnings Management actions taken by the company.

Of course, the company does not want users of financial reports to know about the profit interventions that have been carried out so that the company is more guided by other variables such as the combination of company prospects in the Investment Opportunity Set and social awareness of the disclosure of Corporate Social Responsibility when they want to do Earnings Management. Moreover, earnings management actions depend on the human (managers) motives during the period and also can be impacted not only by internal events but also by external events related to the managers and company. It is quite hard to detect the main factor that drives earnings management actions in a company

6. Conclusion and Suggestion

In accordance with the results from this research, it can be concluded that IOS using Market Value to Book Value of Assets and Corporate Social Responsibility has a greater direct effect than the indirect effect on profitability as proxied by Return on Assets. MVBVA has a positive and insignificant effect on profitability. This means that every time there is an increase in the MVBVA, the ROA will also increase because the company's good growth prospects will certainly be in line with the company's profitability, but the changes that occur in the ROA are not significant because the MVBVA is only an illustration of the company's prospects and there are other circumstances that affect ROA such as asset productivity and the real results of investments made by the company.

The Investment Opportunity Set using Market Value to Book Value of Assets has a greater direct effect than the indirect effect through Corporate Social Responsibility on Earnings Management. Meanwhile, CSR has a smaller direct effect than the indirect effect through IOS as proxied by MVBVA. If the company's growth prospects have shown good value, of course, the company no longer needs to intervene in profits, but the changes that occur in Earnings Management do not really depend on the MVBVA because this proxy is only an illustration of the company's prospects and there are other circumstances that affect Earnings Management such as Profitability and Corporate Tax. Profitability, as proxied by Return on Assets, has a fairly small effect on Earnings Management. Return on Assets as an intervening variable does not mediate the effect of Investment Opportunity Set using Market Value to Book Value of Assets and Corporate Social Responsibility disclosure on Earnings Management.

Results from this research stated that MVBVA has a positive effect on ROA. The good company prospect as shown by MVBVA will give a positive impact on the profitability. Therefore, the company must manage great investment opportunities set wisely and by proving it on the market prices of the companies. CSR has a negative effect on ROA. As we know, the Corporate Social Responsibility programs give a quite big cost for the company during the period and affect the profit generated by the company. But, as feedback, the company will receive a positive impact from society such as a good public image, trust, and support because society thinks the company does not only care about the profit goals but also care about them and the environment.

MVBVA has a negative effect on Earnings Management in banking companies. As discussed earlier, earnings management can be in form of income minimization, income maximization, and even income smoothing. Income smoothing is very common in big companies in order to create stable financial conditions every time. Therefore, the decrease in MVBVA does not mean that there will be an increase in Earnings Management because the profit intervention is based on the manager's goals in creating company performance that they desire for the period.

On the other hand, CSR has a positive effect on Earnings Management. Unfortunately, it is hard to believe that Corporate Social Responsibility activities that have social and moral value for society can also become the company's shield in doing the Earnings Management action. It can happen because the more Corporate Social Responsibility activities done by the company reflects how transparent and careful the company is to the society so it will reduce the suspicion about the Earnings Management action.

In this study, Profitability, as measured by Return on Assets, has chosen to become an intervening variable in the relationship between IOS and CSR on Earnings Management. The result showed that Return on Assets gives quite a small contribution to the relationship between IOS and CSR on Earnings Management and does not mediate the relationship. Return on Assets has been such a common ratio for assessing a company and the managers do not want stakeholders to easily know about the profit intervention. Therefore, managers will rely on other variables before doing the profit intervention.

In order to build great and strong banking companies, companies are advised to be more transparent and not manipulate profits for unilateral purposes in providing financial reporting to interested parties so that users can take the right decisions. Especially, as banking companies are crucial industries for the development of the country's economy and being agents of trust in society, the banking companies must become role-model for other companies to provide reliable financial information for all stakeholders.

The community can provide feedback to companies around them if it turns out that there are economic, environmental, and social impacts caused by the company's presence so that the company can fix them through social responsibility programs. Potential investors, before investing in a company, should be able to pay attention to and analyze the data in the financial reports as a whole, using the company's fundamental techniques in order to provide comprehensive information that is useful in making decisions, especially regarding management intervention on earnings.

There are limitations in this study, it is hoped that further researchers will increase the number of samples and examine other variables that may affect earnings management, and use other company sectors listed on the Indonesia Stock Exchange.

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Earnings Management: Invesment Opportunity Set, Corporate Social Responsibility and Profitability

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Earnings Management: Invesment Opportunity Set, Corporate Social Responsibility and Profitability

Abstract:

Earnings management is defined as management's opportunistic behavior to manipulate earnings according to management's interests. The company's goal is to gain profits, where the company's financial performance is proxied by the company's ability to earn profits. The purpose of this study is to examine and analyze whether Earnings Management is influenced by the Investment Opportunity Set, Corporate Social Responsibility and Profitability and to examine whether the Investment Opportunity Set and Corporate Social Responsibility can affect Earnings Management through Profitability. This study used secondary data with the sample of banking companies listed on Index LQ45 Indonesia Stock Exchange. This study used descriptive and verification analysis methods with analysis tools using path analysis and hypothesis testing. The results of this study indicate that the Investment Opportunity Set and Corporate Social Responsibility have a positive influence on Profitability and Earnings Management, but Profitability as an intervening variable does not mediate the effect of Investment Opportunity Set and Corporate Social Responsibility on Earnings Management. This is because the company sees more aspects other than Profitability as the factor to do Earnings Management actions. Profitability is quite common for investors and users of financial statements in assessing the company's financial performance, so that it is easier for users of financial statements to know the Earnings Management actions taken by the company. However, the company does not want the users of financial statements to know about profit intervention so that the company uses other variables in manipulating earnings such as the Investment Opportunity Set and Corporate Social Responsibility.

Keywords: Investment Opportunity Set, Corporate Social Responsibility, Profitability, Earnings Managemet

1. Introduction

The company's goal is to get the maximum profit possible to attract investors. Generally, investors see profit as the main point as a measure of the success of a company. Investors tend to put funds in entities which have high profits and growth (Dang et al., 2017). A company's profit reflects the company's financial performance, growth prospects and determines the amount of tax that has to be paid. The importance of the meaning of earnings encourages managers to intervene in earnings through "Earnings Management" for certain interests that benefit the company (Becker et al., 1998). Watt and Zimmerman (1990) in Suryani & Herianti (2015) defined earnings management as the action of manager in using accounting policies to report accounting numbers that are not in accordance with the actual economic conditions of the company and mislead investors in making decisions.

There are various financial aspects to intervene profits such as *Investment Opportunity Set* (IOS). The IOS of a company gives influences on the perceptions of managers, owners, investors and creditors of the company (Kallapur & Trombley, 2001). IOS is suspected to be one of the factors that encourage companies to do Earnings Management. If prospect of company shown by IOS showed unfavorable results, of course this will give a negative signal for investors towards the company. Managers usually do not want to lose funds from investors, so they take steps to be able to continue to retain investors, such as manipulating profits to improve the value of the company's prospects in IOS.

Not only from the company's profit and investment prospects that are observed by the public, corporate social responsibility is also a spotlight for assessing a company. Corporate Social Responsibility sees how much awareness the company has about how its business decisions can give impacts on society (Suryani & Herianti, 2015). CSR activities are often used as an excuse for managers to practice earnings management. CSR carried out by the company will provide a positive value for the company because investors do not only look at the financial aspects in the financial reports, but investors also look at the company's image in the public to assess the company's feasibility to get funds. Besides from the prospect of the company and the disclosure of corporate social responsibility, there is one factor that is suspected to encourage the managers to intervene the earnings, which is profitability.

Profitability reflects the organization's capacity to obtain profits during a period and can measure organization's performance. Higher profitability indicates the company's ability to gain profits. Companies that get low profitability in a certain period will be encouraged to carry out earnings management to increase profits or maintain profit stability. Managers often try to manage profits to look good in the investors' eyes so that investors entrust their funds to the company. However, this kind of actions will become misleading false information for investors because the financial reports do not show the real condition of the company.

Based on the above phenomenon, the research problem is whether IOS and CSR have direct or indirect effect on profitability and whether IOS, CSR, and Profitability affect Earnings Management and whether IOS and CSR through Profitability affect Earnings Management. This study aims to examine and analyze: (1) Whether IOS and CSR have direct and indirect effect on Profitability, (2) Whether IOS, CSR and Profitability affect Earnings Management and, (3) Whether IOS and CSR through Profitability affect Earnings Management.

2. Theoritical Background

Investment Opportunity Set (IOS)

IOS is the combination of resources owned and future investment options with positive net present value. Investment options are chances to grow, but sometimes company cannot always use all investment opportunities in future. Companies will have higher expenditures compared to the value of lost opportunities if they cannot use investment opportunities (Astriani, 2014, p. 4). According to Kallapur & Trombley (2001) in measuring company's prospect through IOS, there are three types of proxies namely based on price, investment and variance. In this study, the Investment Opportunity Set is proxied by a price-based proxy, namely Market Value to Book Value of Assets.

Corporate Social Responsibility (CSR)

Corporate Social Responsibility is an action by which organizations keep social concerns in mind for their business activities as well as in their cooperation with partners based on voluntary and associational standards (Nuryana, 2005). The dimension of CSR disclosure is in accordance with the concept of sustainability development in the sustainability report based on the Global Reporting Initiative (GRI G4) standard; there are 91 indicators, which are economic, environmental and social indicators. To make no gap between companies that make sustainability reporting and companies that do not, CSR calculations are carried out using a dummy variable, namely, Score 0: if the company did not disclose item in the indicator. Score 1: if the company disclosed the item on the indicator.

Profitability

Profitability is the organization's ability to obtain profits within a period. There are five proxies in measuring profitability ratio: Return on Assets, Return on Equity, Net Profit Margin, Gross Profit Margin and Earnings per Share as stated by Hamidah (2015, p. 57). In this study used Return on Assets to measure the profitability. Return on Assets is a ratio that shows the rate of return on total assets after profit minus interest and taxes which shows the success of the company's asset performance in a certain period.

Earnings Management

According to Suryani & Herianti (2015), Earnings Management defined as the action of managers in using accounting policies to report accounting numbers that are not in accordance with the actual economic conditions of the company and mislead investors in making economic decisions with the profit figures. Basically, there are three approaches used to detect earnings management, namely the model based on aggregate accruals, specific accruals and distribution of earnings after management (Sulistyanto, 2008). In this study, researchers used the first model based on aggregate accruals using discretionary accruals referring to the modified Jones model as a proxy for earnings management.

Hypotesis Development

Companies with high IOS tend to have a high level of profitability because they are assumed to be able to manage company resources well. The implementation of CSR activities can increase the company's sales and will ultimately increase profitability. On the other hand, the company will get a positive image in the community when the company implements CSR well. This positive image is able to give positive benefits for company.

Research by Sari (2013) related to the effect of IOS on profitability using ROA shows positive and significant effect. Musfirarti et al. (2021) stated that CSR disclosure has a positive and significant effect on profitability using ROA. Based on the description above, the hypotheses in this study can be formulated as follows.

H_1: IOS using Market Value to Book Value of Assets as indicator has an effect on Return on Assets as the profitability indicator.

H_2: CSR has an effect on Return on Assets as the profitability indicator.

Investment Opportunity Set (IOS) of a company reflects the company's future growth projections. The IOS value is expected to show high company growth. When the IOS is low, managers are likely to intervene in earnings which can be detected with Discretionary Accruals to provide a good projection of the company's growth in the future and will give profits for investors. Disclosure of the company's Corporate Social Responsibility (CSR) activities is one of the information disclosures made by the company to third parties through annual financial reports. Earnings Management is the behavior of managers to intervene the net income reported in financial statements for certain purposes by using various strategies such as making CSR activities as the shield.

Research by Irawan & Apriwenni (2021) showed that IOS has a positive and significant effect on Earnings Management while Kumala & Haryono (2004) stated that IOS has no significant effect on Earnings Management. Suryani & Herianti (2015) stated that CSR disclosure has a positive and significant effect on Earnings Management. Research by Purnama (2017) showed that there is a positive and significant effect from Profitability on Earnings Management. Therefore, the research hypothesis can be formulated as follows.

H_3: IOS using Market Value to Book Value of Assets as indicator, CSR and Profitability using Return on Assets affect Earnings Management.

H_4: IOS using Market Value to Book Value of Assets as indicator and CSR through Profitability using Return on Assets affect Earnings Management.

3. Research Methodology

This study used secondary data sourced from the annual financial reports of banking companies on index LQ45 of Indonesia Stock Exchange for 2016-2020 periods. This study used descriptive and verification analysis methods and analysis tools using path analysis to determine the direct and indirect effects. Test the normality of the data and test the hypothesis F and t. Operational variables can be seen below.

Table 1. Operational Variables

Variable	Definition	Formula	Scale
Market Value to Book Value of Assets (X_1)	The development possibilities are showed by market prices (Kallapur & Trombley, 2001).	$\text{MVBVA} = \frac{(\text{T.assets} - \text{T.equity}) + (\text{Stocks x Stocks price})}{\text{T.assets}}$	Ratio
Corporate Social Responsibility (X_2)	An action when organizations keep social concerns in their business activities based on voluntary standards (Nuryana, 2005).	$\text{CSR} = \frac{\text{Total of indicators disclosed}}{91}$	Ratio
Return on Assets (Y)	A profitability ratio that shows return of total assets (Hamidah, 2015).	$\text{ROA} = \frac{\text{Profit after tax}}{\text{Total assets}} \text{x } 100$	Ratio
Manajemen laba (Z)	Earnings management proxy uses the modified Jones model, namely total accruals and regression models to detect overall earnings management (Suryani, 2017).	**Step 1:** $TAC_{it} = N_{it} - CFO_{it}$ **Step 2:** $\frac{TAC_{it}}{A_{it-1}} = \beta_1 \left(\frac{1}{A_{it-1}}\right) + \beta_2 \left(\frac{REV_{it} - REV_{it-1}}{A_{it-1}}\right) + \beta_3 \left(\frac{PPE_{it}}{A_{it-1}}\right)$ **Step 3:** $NDA_{it} = \beta_1 \left(\frac{1}{A_{it-1}}\right) + \beta_2 \left(\frac{\left([REV_{it} - REV_{it-1}] - [REC_{it} - REC_{it-1}]\right)}{A_{it}}\right) + \beta_3 \left(\frac{PPE_{it}}{A_{it-1}}\right)$ **Step 4:** $DA_{it} = \frac{TAC_{it}}{A_{it-1}} - NDA_{it}$	Ratio

4. The Research Findings and Discussion

Findings

Before doing the path analysis test, a normality test was carried out using the Kolmogorov-Smirnov Test, the result of Asymp Sig value is 0,200 > 0,05 then the data is normally distributed so that the data in this study is feasible to use. All correlation coefficient probability values obtained are significant, namely sig. (2 tailed) > 0,05 indicates that the correlation of each variable is a significant relationship. Simultaneous test results MVBVA and CSR have 58,10% contribution to ROA. The results of data processing that tested the effect of MBVA and CSR on profitability based on path analysis obtained a direct effect of MVBVA on ROA is 12,60% and the value of the indirect effect of MVBVA through CSR on ROA is 11,35% and the total effect is 23,95%. The significance value of MVBVA to ROA is 0,069 > 0,05. These results confirm that Ho is accepted and Ha is rejected. Hence, partially MVBVA has no significant effect on ROA.

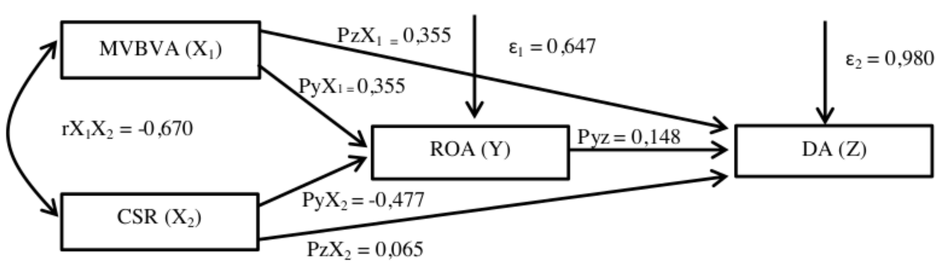
The result of the path analysis of the direct influence of CSR on ROA is 22,8% and the indirect effect of CSR through MVBVA on ROA is 11,35% and the total effect is 34,15%. The significance value of CSR on ROA is 0.018, which is smaller than 0,05, so Ho is rejected and Ha is accepted. Hence, partially partially CSR has a significant and negative effect on ROA. These results indicate that every time there is an increase in social responsibility activities, there will be a decrease in profitability because the more social responsibility activities done by the company it will increase the company's expenses thereby profits will decrease.

The result of data processing that tested the effect of MVBVA, CSR and ROA based on the results of path analysis obtained the direct effect of MVBVA on Earnings Management is 2,2% and the indirect effect of MVBVA through CSR on Earnings Management is 0,65% with total effect is 2,85%. The significance value of MVBVA on Earnings Management is 0,601 > 0,05, so Ho is accepted and Ha is rejected, Hence, partially MVBVA has no significant effect on Earnings Management.

The result path analysis direct effect of CSR on Earnings Management is 0.40% and indirect effect of CSR through MVBVA on Earnings Management is 0.65% with total effect is 1.05%. Thee significance value of CSR on Earnings Management is 0.819 > 0.05, so Ho is accepted and Ha is rejected, meaning that partially CSR has no significant effect on Earnings Management.

From the path analysis also obtained the direct effect of ROA on Earnings Management is 2.20% with significance value is 0.481 > 0.05, then Ho is accepted and Ha is rejected, meaning that partially the ROA variable has an effect and is not significant on Earnings Management. The following can be seen in Figure 1 the influence of MBVA, CSR through Profitability on Earnings Management.

Figure 1. The influence of MVBVA, CSR through ROA on Earnings Management



The influence of MVBVA through ROA on Earnings Management has direct effect $PyX_1.PzX_1.Pyz$ = -0,80%, while indirect effect MVBVA through CSR and ROA on Earnings Management is

$PyX_1.PzX_1.rX_1X_2.PyX_2.Pyz$ = -0,30%. Then, the total effect is -1,10%. The direct effect from influence of CSR through ROA on Earnings Management is $PyX_2.PzX.Pyz$ = -0,50%, while indirect effect CSR through MVBVA and ROA on Earnings Management is $PyX_2.PzX_2.rX_1X_2.PyX_1.Pyz$ = 0,11%. Thus, the total effect is -0,39%. The contribution of the influence of MVBVA through ROA on Earnings Management is -1,10%. The contribution of the influence of CSR through ROA on Earnings Management is -0,39%. Thus, the total effect is -1,49%. Therefore, MVBVA and CSR through ROA gave negative contribution on Earnings Management. It means that Return on Assets as an intervening variable weakens and does not mediate the influence of Market Value to Book Value of Assets and Corporate Social Responsibility on Earnings Management.

Discussion

From the results above, it proved that companies which have good prospects in the future are proxied by the MVBVA and have the awareness and social responsibility programs for the community can give good impact on profitability. This result is in accordance with result from Sari (2013) and Musfirati et al. (2021) that stated IOS and CSR affect profitability as proxied by ROA. The combination of good corporate prospects with disclosure of corporate social responsibility programs does indeed provide positive impact for company in the public and attract investors because a good company prospect means that the company is able to optimally manage its business activities to increase profitability and corporate social responsibility activities make the community give a positive response to the company. Partially, MVBVA has no significant effect on ROA in banking companies, presumably because predictions from company prospects with good value do not always mean high-value company profitability as well as predictions from bad company prospects also cannot determine company profitability because in that period there may be factors other factors that affect the level of profitability, such as leverage, liquidity, and assets turnover.

CSR has a negative effect on ROA because the implementation of social responsibility activities done by the company will increase the company's expenses and have an impact on profits for the period. However, CSR will give positive impact on society that is beneficial for the survival of the company as stated in the legitimacy theory which states that the value system of an entity is the same as the value system of the social system of society where an entity is part of the community. The impact of the company's activities will greatly affect the surrounding community so that what is done by the company will return to the community and again have an impact on the company itself.

The company's prospects as reflected in the MVBVA and the company's social concern for the community from CSR activities do not guarantee that the company will not carry out profit manipulation because it is suspected that there are other factors that can be associated with agency theory (Salno & Baridwan, 2000 in Suryani, 2017). ROA does not have significant effect on earnings management in banking companies, these results support the research conducted by Karina & Sutandi (2019) which stated that the greater the level of ROA does not affect the company's management actions in intervening on earnings. This could happen because banking companies listed on the LQ45 index of the Indonesia Stock Exchange no longer rely on Return on Assets as a determinant of Earnings Management actions.

MVBVA and CSR have a positive influence on ROA and Earnings Management. This shows that profitability as proxied by Return on Assets as an intervening variable does not mediate the effect of MVBVA and CSR on Earnings Management. This is because the company sees other aspects other than ROA as a driver of Earnings Management actions, because ROA is quite commonly monitored by investors or users of financial statements so that it can make it easier for users of financial statements to find out Earnings Management actions taken by the company. Of course, the company does not want users of financial reports to know about the profit interventions that have been carried out so that the company is more guided by other variables such as the combination of company prospects in the Investment Opportunity Set and social awareness of the disclosure of Corporate Social Responsibility when they want to do Earnings Management.

5. Conclusions and Suggestions

Conclusions

In accordance with the results from this research, it can be concluded that IOS using Market Value to Book Value of Assets and Corporate Social Responsibility has a greater direct effect than the indirect effect on profitability as proxied by Return on Assets. MVBVA has a positive and insignificant effect on profitability. This means that every time there is an increase in the MVBVA, the ROA will also increase because the company's good growth prospects will certainly be in line with the company's profitability, but the changes that occur in the ROA are not significant because the MVBVA is only an illustration of the company's prospects and there are other circumstances that affect ROA such as asset productivity and the real results of investments made by the company.

The Investment Opportunity Set using Market Value to Book Value of Assets has a greater direct effect than the indirect effect through Corporate Social Responsibility on Earnings Management. Meanwhile, CSR has a smaller direct effect than the indirect effect through IOS as proxied by MVBVA. If the company's growth prospects have shown good value, of course, the company no longer needs to intervene in profits, but the changes that occur in Earnings Management are not actually caused by the MVBVA because this proxy is only an illustration of the company's prospects and there are other circumstances that affect Earnings Management such as Profitability and Corporate Tax. Profitability as proxied by Return on Assets has a fairly small effect on Earnings Management. Return on Assets as an intervening variable does not mediate the effect of Investment Opportunity Set using Market Value to Book Value of Assets and Corporate Social Responsibility disclosure on Earnings Management.

Suggestions

Companies are advised to be more transparent and not manipulate profits for unilateral purposes in providing financial reporting to interested parties so that users can take the right decisions. The community can provide feedback to companies around them if it turns out that there are economic, environmental, social impacts caused by the company's presence so that the company can fix it through social responsibility programs. For potential investors, before investing in a company, they should be able to pay attention to and analyze the data in the financial reports as a whole, using the company's fundamental techniques in order to provide comprehensive information that is useful in making decisions, especially regarding management intervention on earnings.

There are limitations in this study, it is hoped that further researchers will increase the number of samples and examine other variables that may affect earnings management and use other company sectors listed on the Indonesia Stock Exchange.

Acknowledgment

First of all, the writer would like to express his praise and gratitude to Allah SWT who has given His grace, favors and gifts, so that finally the author can complete this research as a contribution to the development of accounting and finance science. This research is the result of the author's research conducted jointly with a clear division of tasks and responsibilities. The first author as well as the author contributes in analyzing the data and compiling the research results and putting them in an article. Member authors assist the primary authors who contribute to the collection and processing of data.

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